have led to competitors having access to the tools needed to effectively compete. To date, according to a USTA press release, the RBOCs and GTE have spent more than $4 billion to open their markets to competitors.[53] This includes expenditures for operational support systems (OSS), new employees, number portability and other capital expenditures necessary to meet the requirements of new entrants to the local market. Nationally, as of October 1997, ILECs (not including Ameritech) supplied approximately 1147 collocation cages and 3,805 NXX codes. Moreover, approximately 927,443 lines were lost to competitors and 6,476 OSS requests were being processed daily by competitors.

In the Bell Atlantic region, more than 33,000 unbundled loops and more than 175,000 resold lines were in service in October of 1997 along with 200,000 interconnection trunks and 401 collocation sites in Bell Atlantic switching centers.[54] Over 6.5 billion minutes of traffic have been exchanged between Bell Atlantic and its competitors in 1997.[55]

In the Ameritech region, as of August 1997, more than 52,000 unbundled loops and more than 253,361 resold lines were in service along with 73,608 interconnection trunks.[56] Ameritech is provisioning lines to competitors in most of its wire centers with 47 CLEC switches deployed in the region by the end of 1997 and 97 estimated switches being deployed by the end of 1998. With capacity to serve 80,000 lines per switch, by the end of 1998, competitors will have the capability to serve over 7.75 million lines. Currently, competitors are serving 120,000 lines in Michigan, 130,000 lines in Illinois and over 300,000 lines regionwide.[57]

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[53] USTA Press release, October 22, 1997, "USTA Says Bell Companies And GTE Have Spent More Than $4 Billion To Open Their Markets To Competitors."

[54] *Competition Progress Report*, Bell Atlantic, November 13, 1997

[55] This is 1.2% of total Bell Atlantic (both Bell Atlantic and the former NYNEX companies) 1995 local dial equipment minutes according to the FCC's Monitoring Report, CC Docket 87-339, May 1997, Table 4.15. However, it is likely that it represents a much higher percentage of Bell Atlantic revenue.

[56] Statement of Barry K. Allen, Before the Subcommittee on Antitrust, Business Rights, and Competition, U.S. Senate, September 17, 1997.

[57] *Ibid.*

In the BellSouth region, more than 320 CLECs have been authorized to provide service including 41 CAPs that have switching capability.[58] As of August 1997, more than 4,000 unbundled loops and 79,000 resold lines were in service. The data from BellSouth provide a vivid example of how competitors are targeting select geographic areas that provide disproportionate amounts of revenue; 76 percent of resold lines and 65 percent of unbundled loops are concentrated in just two states.[59]

In the SBC region, there are more than 330,000 access lines connected to CLECs including 184,000 resold lines.[60] More than 86,000 CLEC interconnection trunks are operational including 390 E-911 trunks. Also, there are more than 2300 and 60 CLEC T-1 and T-3 facilities, respectively.

More significant are the growth rates: in the Bell Atlantic region, unbundled loops and minutes of use have doubled since January 1997, while resold lines grew by a factor of over seven.[61] In the Ameritech region, since January 1997, unbundled loops have practically doubled, resold lines grew by a factor of twelve and CLEC lines in the region grew by a factor of over four.[62] In the SBC region, in September 1997, 57,000 access lines were converted to resale and 12,000 to 15,000 orders were being processed weekly.[63] In Texas, there was a 140 percent increase in resold lines from June to August 1997.[64]

These facts are significant because the absence of barriers to growth means that the availability of UNEs can make many ILEC customers potential CLEC customers. Therefore,

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[58] Comments of BellSouth, *In the Matter of Commission Actions Critical to the Promotion of Efficient Local Exchange Competition*, CCBPol 97-9, August 11, 1997.

[59] *Ibid.*

[60] Information for SBC comes from http: intranet.sbc.com/SBCWIN/news/insight/issue002/is_2L6.html or is_page2.html or is_2L8.html.

[61] *Competition Progress Report*, Bell Atlantic, September 26, 1997.

[62] Statement of Barry K. Allen, Before the Subcommittee on Antitrust, Business Rights, and Competition, U.S. Senate, September 17, 1997.

[63] http: intranet.sbc.com/SBCWIN/news/insight/issue002/is_2L6.html.

[64] *Ibid.*

competitive forces can grow quite rapidly, and delaying ILEC price flexibility can have devastating distortionary effects on the market. Delay is particularly troublesome because the first customers to switch suppliers represent higher than average revenues and lower than average costs.

Market forces are sufficiently developed in the special access and dedicated transport markets to constrain ILEC pricing to determine optimal levels of output, investment and price. There is no need for regulation in these markets because these are high volume services for which entrants have been aggressively competing, are offering innovative pricing plans to customers and are not constrained when introducing new services by unneeded regulatory requirements such as tariffs or public interest tests. These competitors are large and powerful organizations, such as WorldCom-MFS, ACSI and Brooks Fiber that have the flexibility to tailor services to customer-specific demands.[65] In addition, special access and dedicated transport customers are large organizations such as AT&T, MCI and Sprint that have the resources and economies to self-supply special access and dedicated transport efficiently if they are unable to obtain cost-based prices for these services.

Moreover, the Commission's Expanded Interconnection proceedings in the mid-1990's permit competitors to terminate their own special access and switched transport access transmission facilities at ILEC central offices, greatly increasing the ability of competitors to combine their own transport facilities with ILEC switches and loops to compete effectively in these markets. There is simply no danger of ILECs exerting market power in the markets for special access and dedicated transport—because they have none. Therefore, regulation is not necessary. While competition is developing at different rates in the remaining carrier access markets, the Commission should realize that the degree of competition is also likely to vary across geographic areas and among particular customers. For this reason, many switched

[65] As an example of the lack of barriers to entry and growth, Brooks Fiber reported a year-over-year local service revenue increase of 230% and an increase over last quarter alone of 35%. ACC, a New York CLEC with plans to expand to Pennsylvania and Massachusetts, reported its revenue from local and other services increased over 58 % versus a year ago, see Bell Atlantic and NYNEX Comments, *In the Matter of Commission Actions Critical to the Promotion of Efficient Local Exchange Competition*, CCB Pol. No. 97-9.

access services are ready for immediate removal from price cap regulation. Market power is exercised and thus properly measured in specific product and geographic markets, not in national aggregates. A closer examination, conducted market by market, is likely to reveal that the ILEC is not the sole provider and that, in many areas and for many customers, competition is sufficiently developed to remove the remaining services from asymmetric regulatory restrictions.

B. FCC Efforts to Eliminate Perceived Barriers to Entry

The Telecommunications Act of 1996 and a series of subsequent Commission orders to implement the 96 Act greatly increased the ability of other carriers to compete.[66] As a result, interconnection agreements and the mandatory provision of UNEs at cost-based rates reduce the amount of sunk costs[67] required to enter the local exchange and carrier access markets. Under the terms of the Interconnection Order, UNEs may be combined, by any competitor, to provide a carrier access service that is equivalent to conventional access service—provided that the competitor "wins" the end user.[68] This ability allows a CLEC, for example, to purchase unbundled loops, local switching, signaling, and transport to provide carrier access so that the competitor need not invest in loops, switches or transport to provide carrier access. In addition, while in the past access customers were able to bypass ILEC carrier access services through self-supply or obtaining alternative CAP services, UNEs and interconnection agreements now have the effect of increasing alternatives to traditional ILEC carrier access services. UNEs and interconnection agreements facilitate competitive entry by making it economical for

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[66] See note 1 above.

[67] In this context, sunk costs are defined as costs that must be incurred to enter a market but which cannot be recovered if the firm elects to leave the market. All else equal, if an entrant has to incur significant sunk costs, it will be reluctant to enter a market because it could not recoup those costs if its enterprise failed. Resale and the mandatory availability of UNEs means that entrants into the carrier access and local exchange markets do not have to incur the sunk costs of constructing a local exchange distribution network but can use the ILEC's facilities instead.

[68] The requirement that a competitor must "win" the end user in order to compete for access exists because some of the UNEs that are required in order to provide carrier access are dedicated facilities. For example, loops and switching ports are required to provide carrier access but they are dedicated to the end user. A competitor must convince the end user to switch to it in order to obtain the unbundled element.

competitors to enter in geographic areas that may have been unremunerative—for reasons such as insufficient density and volume to warrant investment in facilities—prior to passage of the Act. The Commission has consistently recognized this substitutability between UNEs and carrier access services.[69]

The main effect of the interconnection agreements with UNEs at cost-based rates is to reduce barriers to entry into the local exchange and exchange access markets so that most ILEC customers become potential CLEC customers, provided the CLEC can convince customers to switch. Though competitive alternatives will still come first to high-volume customers in high density areas, most ILEC customers are vulnerable to competitors. Thus, these markets have been fully opened to competition, and the presence of interconnection agreements should give the Commission a sense of urgency to remove barriers that prevent market forces from substituting for regulatory constraints. As of July 1, 1997 there were 1,231 interconnection agreements between ILECs and CLECs. As Figure 2 below indicates, these agreements are fairly evenly distributed throughout the country. They are not clustered in a particular region or concentrated in large states.

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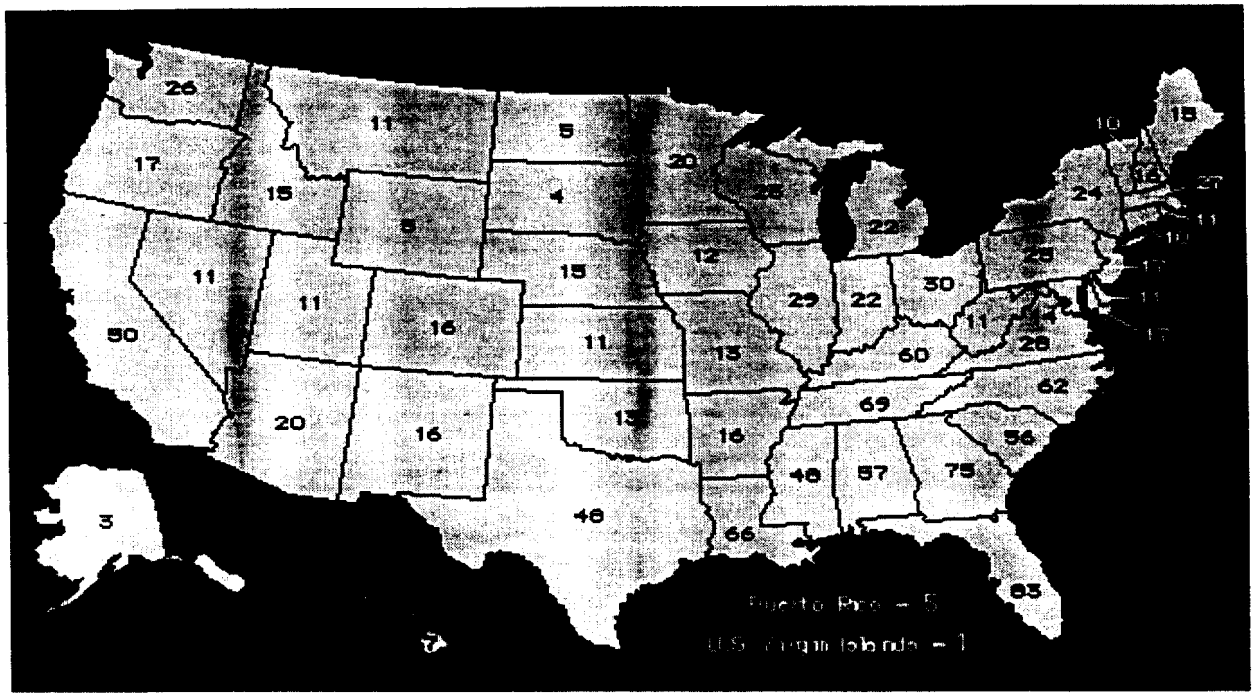
[69] The Commission has recognized on various occasions that UNEs can be an effective substitute to the current Part 69 carrier access elements. First, in its pricing decision in the Interconnection Order, the Commission temporarily permitted the ILECs to recover CCL charges and the Transport Interconnection Charge (TIC) from purchasers of UNEs, because it was concerned with the substitutability between UNEs and carrier access and the role carrier access has historically played in promoting universal service. Second, in the access reform Notice of Proposed Rulemaking (NPRM), the Commission characterized UNEs as being a "ubiquitous substitute for access services." (NPRM in CC Docket No. 96-262, December 24, 1996 at ¶170). Finally, the Commission's Access Reform Order relied heavily on the use of UNEs as substitutes to carrier access:

> The new competitive environment envisioned by the 1996 Act threatens to undermine this [access charge] structure over the long run. The 1996 Act removes barriers to entry in the local market, generating competitive pressures that make it difficult for incumbent LECs to maintain access charges above economic cost. For example, by giving competitors the right to lease an incumbent LEC's unbundled network elements at cost, Congress provided IXCs an alternative avenue to connect to and share the local network. Thus, where existing rules require an incumbent LEC to set access charges above cost for a high-volume user, a competing provider of carrier access services entering into a market can lease unbundled network elements at cost, or construct new facilities, to circumvent the access charge.(Access Charge Order at ¶32).

Thus, as it implements the Act, the FCC has consistently taken the view that the availability of UNEs provides forceful discipline on the ILECs' pricing of carrier access services.

FIGURE 2 –NUMBER OF INTERCONNECTION AGREEMENTS BY STATE AS OF JULY 1, 1997



Source: USTA

The recent Eighth Circuit Court of Appeals decision regarding the Commission's Interconnection Order clarifies that CLECs can recombine UNEs but that ILECs are not required to recombine them.[70] The decision thus does not change the fact that competitors have access to substitutes for ILEC switched access using the ILEC network at cost-based rates, as determined by negotiation or ultimately by state regulators. Once UNE rates are established, competitors can use them individually or in combination to provide effective alternatives to current services.

Market conditions have developed to the point where some degree of pricing flexibility

[70] *Iowa Utilities Board v. FCC*, Nos. 96-3321, et. al. (8th Circuit July 18, 1997).

in most carrier access markets is required. As discussed above, special access and dedicated transport markets are sufficiently developed to the point where continued pricing and tariffing constraints serve no worthwhile purpose and are in fact anticompetitive. UNEs facilitate entry into the market by eliminating the sunk costs of constructing a ubiquitous network, which substantially reduces overall barriers to entry. Because these markets are subject to entry with low sunk costs, efficient competition requires symmetry in the regulatory treatment of entrants and the incumbent so that customer satisfaction determines the market outcome rather than the tilt of arcane regulatory procedures. As a result, services which meet these characteristics should be identified and removed from price cap regulation. For those remaining carrier access services where competitive forces are still developing, an objective and clear process should be established by the Commission to implement additional levels of pricing flexibility as competition evolves.

IV. RELEVANT ECONOMIC GUIDELINES

A. Importance of specific, identifiable and quantifiable triggers

Pricing and regulatory flexibility has historically been absent in the carrier access market.[71] While some of the regulatory requirements mentioned above should have been eliminated in the past irrespective of the potential or actual state of competition—e.g., geographic averaging of access rates—the current economic and regulatory environment compels the Commission to establish a process that will phase out redundant regulatory requirements that constrain pricing flexibility as competition increases. Our fundamental recommendation is that even though there is no economic "bright line" for moving between phases of flexibility, the need still exists for objective criteria so that regulation decreases as competition increases. This process should be established only to handle those remaining

[71] While waivers from particular FCC rules could be requested, carrier access prices were generally set equal to their fully-distributed accounting costs as determined by Part 69 of the Commission's rules. Seven years of price cap regulation has helped to rationalize the pricing of some access elements, but, in general, there has been little relationship between access element prices, market conditions or economic costs.

carrier access services where competitive forces are not sufficiently developed to constrain prices and to lead to eventual deregulation.

Weighing the costs and benefits of implementing regulatory flexibility is much simpler in the abstract than in the real world. Generally, telecommunications markets are neither perfectly competitive nor perfectly regulated, and the correct question is therefore not whether a given firm can exercise excessive control over price in a given market but whether the benefits of a proposed regulatory modification will outweigh the costs in the "imperfect" markets in which telecommunications services are sold and regulated. The question regulators need to answer is not whether ILECs have any market power,[72] but rather how much control over market price is too much and thus requires continued price regulation?

While there is general agreement on the indicia of competition in a market, there is likely to be no agreement in a litigated case concerning the degree of control over price that should trigger reduced regulatory constraints. For example, how much weight should be given to the absence of entry barriers as compared with the absence of entry? To what extent does the threat of potential entry discipline the pricing of a firm with a large market share? Can switched trunk-transport and special access be treated as belonging to the same relevant market? While economists can perform quantitative studies of these issues, the determination of the effect of any proposed change in regulation on price, output, investment and service quality will inevitably require judgement on the part of policymakers. Given that economic theory supplies no clear and unequivocal answers and considering the difficulty involved in measuring competition precisely, especially in an adversarial setting, it is important that readily available and easily verifiable criteria be used by policymakers. The triggers that are used to remove successive regulatory restrictions must be known, measurable, and observable to decrease the likelihood that unneeded asymmetric regulations and regulatory proceedings will distort the competitive process.

[72] We generally do not regulate prices in concentrated and imperfectly competitive markets such as soft drinks, even though large firms provide differentiated products and have some control over price.

While economics provides no clear and unequivocal answers to the question at hand, economic theory does provide important insights which, when combined with objective criteria, can be used to determine the pace of regulatory reform. For firms to exercise market power, two conditions must hold: (i) there must be little competition from existing firms producing substitutes for the service in question; and (ii) entry into the market by new competitors must be blocked by significant legal or economic barriers.

Although market concentration is a proper starting point for evaluating alleged market power, care must be taken not to equate market share with market power. Basing an analysis on market share or concentration is likely to lead regulators astray because current market share is fundamentally backward looking and fails to put sufficient weight on current and future developments.[73] While this tends to be the case in general, it is particularly harmful in technologically dynamic markets like telecommunications. As one FCC staff member has observed,

> Given the technology of the telecommunications industry, many markets will probably be characterized by the presence of one or more firms with a predominant market share. Under well-accepted precedent, this basic condition alone does not indicate that a market is performing poorly. This is why, in the context of telecommunications, the analysis must always move beyond [market concentration] and toward the evaluation of the elasticities of supply and demand and, in particular, the presence (or lack) of barriers to entry.[74]

More important than market concentration is the requirement that consumers have choices available to them. For this reason, when analyzing market power it is important to look at the productive capacity available from competitors. As recognized by the Commission in its AT&T Non-Dominant Order, the appropriate measure of size for network-based telecommunications markets is generally capacity.[75] For carrier access markets, capacity

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[73] A more insidious problem is that shares are frequently calculated for things other than markets. For telecommunications services where a small number of customers are responsible for a large fraction of demand, a high average share can conceal low market shares in the economically relevant markets.

[74] L.J. Spiwak, "Reorienting Economic Analysis of Telecommunications Markets After the 1996 Act," *Antitrust*, Spring 1997 at 34.

[75] *In the Matter of Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd 3271, (continued...)

measures must be tempered by addressability. That is, if rivals have capacity available that can "address" a significant number of customers and that can be brought on line at low additional cost, the ILEC cannot exercise market power, and therefore, regulatory constraints should adjust accordingly.

After an analysis of current competition, attention generally turns to conditions of entry into the market.[76] Absent barriers to entry, any elevation of price above the competitive level would attract entry, expand market supply and reduce the market price towards the competitive level. Entry barriers, therefore, are a necessary condition for market power. A thorough analysis of entry conditions must include evaluation of the extent of sunk costs of entry. In evaluating market power, sunk costs are key to measuring barriers to entry. If sunk costs are not important requirements of entry, competitors can enter and exit the industry at relatively low costs to take advantage of any profitable opportunities in the market. Therefore, to assess the conditions of entry in the relevant market, the Commission should analyze the extent of legal and regulatory barriers to entry and characterize the degree to which entry (or exit) would entail commitment of sunk costs for potential entrants. If entry has taken place at all, entry barriers could not have been insurmountable.

In implementing these guidelines, two additional considerations should be observed. First, the availability of interconnection agreements, UNEs at cost-based prices, and resale have reduced the level of sunk costs required to enter the local exchange and carrier access markets, and prospective regulatory policy must take into account this reduction in entry barriers. Second, when evaluating the state of potential and actual competition, it is important that measurement be made in a properly defined economic market. For local exchange and carrier access services, geographic markets are generally small, since particular customers cannot travel to obtain services. For practical purposes, market areas can be defined by common

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(...continued)

(1995).

[76] Of course, if current competition is sufficient to rule out the exercise of market power, it is not necessary to consider barriers to entry.

social, economic and general business characteristics or by ILEC network geography or architecture. The speed and direction of competition will vary geographically, at least initially, and efficient competition will likely be sacrificed if this factor is ignored.

B. Triggering Regulatory Relief

The preceding section reveals that while economic theory provides important and useful insights to assist the Commission, judgment on its part will be required. For this reason, clear and objective triggers that are easily measured and verified can reduce contention and allow regulators to expedite proceedings to provide additional pricing flexibility and reduce regulatory constraints. On the other hand, for some services, e.g., special access and dedicated transport, prices are already sufficiently constrained by market forces so that triggers would be unnecessary.

A well-crafted plan should link regulatory relief—such as volume and term discounts, contract tariffs and forbearance—to objective triggers that measure the availability and use of competitive alternatives to ILEC carrier access. Regulatory relief can be structured in different phases, in which, for example, certain types of triggers may correspond to different forms of regulatory relief. But in general, triggers can be thought of as market symptoms which, combined with the availability of UNEs, makes actual competition more viable and potential competition a greater check on the ability of the ILEC to raise prices above the competitive level. Triggers are a means for regulators to ease regulatory constraints in particular markets—in certain market areas or for certain services and customers—as the ILECs' residual market power is reduced to levels found in unregulated markets. In this sense, triggers work to ensure that once market conditions change, appropriate regulatory constraints immediately follow. Their use ensures that there is a timely process in place that responds to the rapidly-changing market conditions in carrier access and increases the likelihood that efficient regulatory decisions are implemented.

Examples of potential triggers include availability of unbundled network elements, transport and termination charges in place, provision of network elements and services, and the existence of number portability arrangements. These objective and easily verifiable triggers

provide useful information regarding the state of regulatory and legal entry barriers. They also contain information about the economic barriers to entry as well, because the availability of UNEs reduces concerns about sunk costs of entry. Additional possible triggers include answers to questions such as the following: Are competitors collocated in wire centers?; Are competitors deploying facilities and using UNEs in the wire centers?; How many competitors are present in some geographic area?; Do competitors have the ability to provide service to a substantial percentage of the market, using their own facilities or those of the ILEC?

In addition, since the purpose of the triggers is to permit ILECs to move between phases of regulatory reform in a manner that matches market conditions, we believe that movements between whatever phases are eventually chosen by the Commission need not be sequential. Meeting the trigger conditions for a particular phase should be sufficient to grant the associated regulatory relief. For example, market conditions for special access services in most geographic areas are such that immediate regulatory forbearance is warranted, and stepping through sequential phases of deregulation would be an inefficient, time-consuming path to ultimate regulatory forbearance.

The key to using objective triggers is that they be easily verifiable and used expeditiously to evaluate ILEC proposals for flexibility. A process that automatically grants ILECs certain regulatory relief when a specific trigger is reached greatly reduces contention, which allows the Commission to administratively expedite ILEC filings. It also prevents the proliferation of ILEC waiver requests, forbearance petitions etc. which could tie up Commission resources. The requirements necessary for regulatory flexibility would have been decided *ex ante*, and thus the Commission's main task would be to verify the fulfillment of the trigger. The importance of moving rapidly to determine the legitimacy of ILEC claims cannot be overstated. Market dynamics are changing the technology and structure of telecommunications at an extremely rapid pace. Having in place quantifiable triggers that correspond to predetermined flexibility reduces uncertainty of the participants and increases the likelihood that competition will not be distorted by unneeded asymmetric burdens.

V. CONCLUSIONS

Since competitive market forces are vastly superior to administrative regulation, the Commission should immediately permit the market to constrain ILEC prices in special access and dedicated transport, where such forces are already strong. Doing so would lead to more efficient pricing, production, and investment. As the Commission embarks on the process of moving remaining carrier access markets to eventual forbearance, it should consider the significant costs to consumers and to society as a whole of not relying on market forces. In order to increase the likelihood that efficient competition develops, the Commission must pursue a policy that regulates ILECs and entrants as symmetrically as possible and that does not attempt to guarantee competitors' success in the marketplace. Though market pressures have influenced carrier access pricing since 1984, the recent removal of entry barriers in the carrier access market stemming from implementation of the Telecommunications Act makes regulatory relief imperative. In our experience, four economic principles are particularly important:

- Imperfect competition is generally far superior to imperfect regulation in controlling ILEC prices and service quality. The potential costs of permitting pricing flexibility for incumbent firms prematurely are small and are likely to be swamped by the benefits of competition under symmetric regulatory conditions.
- Delay is costly. The potential costs of permitting pricing flexibility for incumbent firms prematurely are swamped by the potential costs of inefficient entry from opening markets to competition under asymmetric regulation.
- Competition is important; competitors—incumbents and entrants alike—are not.
- Prices cannot be set solely by reference to cost studies performed in litigated proceedings. Prices should approximate their market levels under competitive conditions, in which both cost and demand factors play a role.

In using these abstract policies in a litigious world, regulators would be well-served by setting *ex ante* observable and measurable triggers that provide specific relief from regulatory obligations, as ILEC services move to different phases of regulatory relief and eventual forbearance.

ATTACHMENT 5

USTA Comments
CCB/CPD 98-12
March 18, 1998

Presentation of Roy M. Neel
President and CEO of the
United States Telephone Association
FCC En Banc on Local Competition
January 29,1998

I am Roy Neel, President and CEO of the United States Telephone Association.

I am pleased to participate today. But I am the only representative from the incumbent Local Telephone industry. So, I'm also a bit apprehensive.

The telecommunications industry is fast paced. It changes every day. It is a fact of life for trade association types like me that we can't even begin to keep up with everything that is going on in the states, cities, and towns. It's hard enough keep track of what's happening at the FCC and the Congress. Still, I will do my best today to give you a ten minute picture of how local competition is shaping up.

But before I do so, I want to make a plea that you have heard before from USTA. The FCC cannot make the decisions it needs to make -- it cannot lead in the transition to competition -- if it does not have the facts. We believe that the FCC can and should adopt simple, non-burdensome reporting requirements for all carriers -- incumbents and new entrants alike. That is the only way to get beyond anecdotes and rhetoric. Remember, even today's forum can only give you a snap shot -- and then only from a few participants.

And you cannot rely only on ILEC data. We only see part of the picture. USTA's members simply don't know how much growth -- both in lines and traffic -- new entrants are seeing from their customers. We can only estimate the volume of services that carriers with facilities networks -- including the Competitive Access providers -- are providing. I ask you to adopt some simple requirements that apply to everyone so that you can base your assessments about competition on up-to-date facts.

This issue was one that USTA included on its list of actions the FCC could take to promote competition. The Commission has made good progress on several items on the list, including numbering administration and reform of the enforcement process. We appreciate your hard work. But action is still needed in other areas.

Now, I want to begin with a few facts about USTA's thousand-plus members. Those members include all five Regional Bell Companies as well as GTE in our Large Company Group.

We have 25 companies who are mid-size members of USTA. The largest is Southern New England, serving 2 million lines and the smallest is Mankato Telephone Company in Minnesota.

The vast majority of USTA members -- over seven hundred of them -- are small companies. They typically serve 5,000 customers or less in a rural area of the country.

Every year, USTA publishes a list of the largest 150 local telephone companies. In this year's list, number 150 has just over 9,000 lines. That gives you some understanding of the size of the hundreds and hundreds that are smaller.

Over 400 incumbent local telephone companies provide cable TV services.

Over 200 of USTA's member companies are involved in some aspect of the long distance business. And more companies are entering that market each day.

More and more local telephone companies, large and small, are becoming Internet access providers. Our estimate -- growing every day -- is that 250 USTA members are in the Internet business.

More than 500 local telephone companies have cellular interests. Many were winners in the auctions for Personal Communications Services Spectrum. Several of them, including EATEL in Gonzales, Louisiana, have launched their PCS offerings in the past couple months.

In information they sent us for USTA's latest membership directory, over 80 companies indicated they now have CLEC operations. It is not at all uncommon for a USTA member these days to be an incumbent LEC, a CLEC, a video provider, a long distance provider, and to have some wireless interests.

Now that I've given you some feel for diversification by the local exchange carriers, I'll move on to the broader local telephone market.

The 1996 Act requires incumbent LECs to take dramatic steps to open their markets to competition, and they are doing so.

Throughout the nation, more than twenty-four hundred (2400) interconnection agreements have been signed between incumbent LECs and their wireline and wireless competitors.

There are Competitive Local Telephone Companies certified in all 50 states and the District of Columbia. Over twelve hundred (1200) certificates have been issued across the nation, with hundreds more pending.

In July, State Telephone Regulation Report listed more than thirty CLECs who hold certificates in five or more states.

Certificates are interesting, but just because a carrier is certified in a state does not mean it has plans to serve statewide.

But USTA's research shows that competitive telecom providers have announced plans to offer service in nearly 800 cities.

Competitive Access Providers have fiber networks in operation in over 300 cities and towns. Many of these networks have been in place for a number of years. In fact, there was a competitive network in New York City prior to divestiture.

In order to serve local customers, you need to give those customers telephone numbers -- and more than six thousand telephone exchanges have been assigned to competitors.

The Regional Bell Operating Companies and GTE alone are spending $4 billion to open their networks to new entrants in the local telephone market.

These funds have been spent on operational support systems, new employees, number portability, and the other capital expenditures necessary to meet the requirements of the Act.

The four billion does not include the capital spent by the nation's other 1,000 local exchange carriers. For example, one of USTA's mid-size members, Cincinnati Bell, has spent $30 per access line just to fulfill its Local Number Portability obligations.

The largest six ILECs now process more than 8,000 competitive orders daily. These companies have dedicated over 8,000 employees to tasks like implementing OSS changes, serving as the CLEC point of contact, processing orders, implementing number portability, and making the network changes for unbundling.

USTA's members have also established about 1600 collocation arrangements.

Incumbent LECs have lost more than one-and-a-half million telephone lines to competitors, practically all lucrative business customers.

Another measure of the growth in competition is the amount of traffic exchanged between incumbents and new entrants. The figures for just three of our largest members and two mid-size companies total nearly 22 billion minutes of traffic exchanged in 1997.

Now, I'll give you some illustrations from company-specific data.

In the Bell Atlantic region, more than 35,000 unbundled loops and more than 208,000 resold lines were in service by November of 1997, along with 212,000 interconnection trunks and 401 collocation sites.

Ameritech has now provided more than 70,000 unbundled loops and 95,000 interconnection trunks. Currently, competitors are using Ameritech services and facilities to serve over 230,000 lines in Michigan, 240,000 lines in Illinois -- almost 600,000 lines regionwide. This does not include lines provisioned by the CLECs on their own facilities.

Ameritech has provisioned lines to competitors in most of its wire centers, with 47 CLEC switches deployed. By the end of this year, Ameritech expects that number to grow to 97 CLEC switches. With capacity to serve 80,000 lines per switch, competitors will be able to serve almost 8 million lines in the Ameritech area.

In the BellSouth region, more than 320 CLECs have been authorized to provide service, including 41 with switching capability. More than 8,000 unbundled loops and 211,000 resold lines are now in service. The data from BellSouth provide a vivid example of how competitors are targeting select geographic areas; 76 percent of resold lines and 65 percent of unbundled loops are concentrated in just two states.

BellSouth has also lost 3 million lines to intraLATA toll competitors.

In the SBC region, there are more than 520,000 lines being resold by CLECs. More than 174,000 interconnection trunks between SBC and CLECs are operational. Also, there are almost 2400 CLEC hi-cap lines in service.

The raw numbers are interesting, but the growth rates may be more significant. In the Bell Atlantic region, unbundled loops and minutes of use have doubled since this time last year. Resold lines grew by a factor of over seven.

In the Ameritech region, unbundled loops have practically doubled in one year, resold lines grew by a factor of twelve and CLEC lines in the region grew by a factor of over four.

In the SBC region, in September 1997 alone, 57,000 access lines were converted to resale. SBC is now processing 12,000 to 15,000 orders weekly. In Texas, there was a 140 percent increase in resold lines from June to August of 1997.

I mentioned that more than 80 USTA members have CLEC operations. Obviously, USTA's members are competing with one another for local customers. For example, both Citizens Telecom and U S WEST are competing for customers in BellSouth's traditional service area. ALLTEL is now offering one-stop shopping in Jacksonville, Florida. Consolidated Communications is an aggressive competitor to Ameritech. And SBC is offering customers in Texas an alternative to GTE.

With me today is Frank Hilsabeck, Chairman of Aliant Communications in Lincoln, Nebraska. Frank is also USTA's Chairman this year. His mid-size company provides wireless, long distance, and Internet Access service. Aliant also now has a statewide CLEC operation, competing with U S WEST.

My favorite example -- and one you may have read about -- is a small telephone cooperative in Montana that built facilities and successfully competed with U S WEST in Terry, Montana. Mid-Rivers Telephone Cooperative BUILT both telephone and cable television network facilities. According to Telecommunications Reports, Mid-Rivers has signed up "most" subscribers in Terry both for telephone and cable service.

Competitors have been very successful in capturing significant special access lines. They have also substituted hi-cap lines for switched access to serve high-volume businesses. These competitive forces were significant even before the Telecommunications Act -- CAP and CLEC revenues doubled between 1995 and 1996.

CAP investment in fiber is growing at a significantly faster rate than that of the ILECs. By the end of 1996, the CAPs' aggregate percentage growth rate was almost seven times that of the ILECs.

GTE, for instance, reports that as of August 1997, approximately 20,000 DS-1 facilities were provided by CAPs in GTE markets.Total GTE DS-1's were about 100,000. So the CAPs have almost 20% of the market.

A 1995 study commissioned by SBC showed that in the Dallas and Houston markets, SBC had already lost approximately 41.2 and 31.6 percent, respectively, of the high capacity special access market. ILECs' high capacity service losses to competitors were as high as: 39 percent in Philadelphia, 35 percent in Pittsburgh, 32 percent in Washington, DC, 27 percent in Baltimore, 39 percent in Los Angeles, 37 percent in San Francisco. By March 1995, CLECs and CAPs had captured 10-15 percent of the nationwide carrier access market.

The trend has continued. By the third quarter of 1996, competitors had captured 55.2 percent of the high capacity market in Chicago and 53.5 percent in Midtown Manhattan.

Another important indicator of the state of local competition is how investors view the new entrants. I know my time is running out, but here are just a few facts in that regard.

James Henry of Bear Sterns says, "The CLECs are successfully competing for a share in the local telephone market, which has been thrown wide open... CLECs are among the best positioned segment of the telecom service industry... and should be core holdings of any telecom portfolios." He says CLEC investors should be rewarded by significant price appreciation.

Tim Horan of Robertson Stephens says, "ILECs will lose 5 percent of their market share per year. The CLECs should capture a significant portion, translating into at least $3 billion per year in incremental revenues." Mr. Horan also points out that the CLEC stocks he covers are up more than 200 percent after the past nine months, driven by strong fundamentals.

Merrill Lynch expects CLEC lines to double in 1998 to three million lines and be five million in 1999. Merrill Lynch is also predicting that CLEC revenue and market share will double in 1998 from 2.6 percent to 5.1 percent and then another significant increase in 1999 to 7.6 percent.

I know that I've used up my time. Again, I appreciate the opportunity to give you a "snapshot" of competitive developments in the local market.